CTOBER 1953

business review

L RESERVE
OF
ELPHIA

UTUAL SAVINGS BANKING

ings banks stimulate thrift and direct money into investment.
pite new problems and intense competition,
thrive so long as they meet the needs of many small savers.

S IN THIRD DISTRICT STATES

payments in 1952 climbed to a new record.
me here continues above the national level.

TAX CHANGES AND TAKE-HOME PAY

Many individuals will have no increase in their take-home pay, when income taxes are cut and Social Security payments rise.

CURRENT TRENDS

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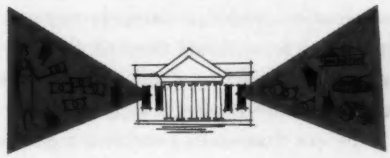
MUTUAL SAVINGS BANKING



About $26.5 billion in assets and 20 million depositors—this in a nutshell describes mutual savings banking in the United States today. The total assets figure testifies to the fact that mutual savings banking is a big business indeed; but the 20 million depositors show that the industry is

bank movement. In the early years of the nineteenth century, when the Industrial Revolution was gaining momentum, many people among the laboring groups found that for the first time their incomes were large enough to permit the thrifty to set aside something for the proverbial "rainy day." In addition, the growing pains of industrialization tended to increase the need of the individual for a liquid fund of savings. An institution that would meet the savings requirements of the lower-income groups was needed—specifically one that would provide a high degree of safety and liquidity and at the same time afford a return to the saver.

But the need for such savings institutions was not enough. New enterprises, no matter how commendable in purpose, come into existence only as the result of promotion. And promotion will normally be found only when the prospect of profit is strong. Since there seemed to be very little hope of profit in institutions catering to the savings needs of low-income groups, the organization of savings banks was undertaken by groups of socially conscious citizens of the community. In keeping with the underlying purpose of the mutual savings banks, these organizers, who later acted as "managers" or "trustees" for the banks, served without pay

In addition to meeting many of the needs of the small saver, there is another equally important side to mutual savings banking—the flow of funds back into the spending stream. Mutual savings banks transfer the savings of their customers into the building of houses, factories, machinery, and tools. In performing these functions, they contribute to economic growth and consequently to a rising standard of living. Of course, mutual savings banks are not alone in performing these functions today, but they were the first institutions in this country to devote themselves primarily to this task.

North of Baltimore and east of Buffalo

The picture of growth, illustrated in the chart, is more significant when it is realized that mutual savings banks are found in only 17 of the 48 states. Furthermore, 87 per cent of the assets are concentrated in only four states—New York, Massachusetts, Connecticut, and Pennsylvania. As of the end of 1952, New York was far ahead with $14.8 billion in assets (58 per cent of the total), followed by Massachusetts with $4.1 billion (16 per cent), Connecticut with $1.7 billion (7 per cent), and Pennsylvania with $1.4 billion (5 per cent). This is why mutual savings banks are often said to be located "north of Baltimore and east of Buffalo."

The concentration of mutual savings banks in the eastern part of the nation results from several factors. Probably most important is the fact that at the time the movement got under way the conditions tending to foster such institutions were found in the industrialized East. As these conditions developed elsewhere other types of financial institutions, mainly commercial banks and savings (or building) and loan associations, stepped in to provide many of the services that savings banks supplied.

The "typical" mutual savings bank

The 528 mutual savings banks operating in the United States range in size from less than one-half million to over one billion dollars in total assets. In addition, policies relating to types of assets held, methods of computing interest-dividends, etc., vary widely among banks. Because of this diversity in size and character it is dangerous to generalize by referring to the "typical" mutual savings bank. For illustrative purposes, however, such a generalization is useful.

What are some of the characteristics of the typical mutual savings bank? Probably the bank is between 50 and 100 years old and is located within 300 miles of New York City; it is under the general supervision of a board of trustees or managers, about 15 in number, who for all practical purposes serve without pay and are among the leading business and professional men in the community. The board initially consisted of the bank's organizers, and vacancies have been filled by vote of the remaining members. The board has delegated authority to a group of officers consisting of a president and various and sundry other officials, including several vice presidents, a treasurer, assistant treasurers, and so on. Bank operations are under the supervision of these officers. In a well-run institution, they are a busy group of people.

Balance sheet of the "average" mutual savings bank

Further insight into the nature of present-day mutual savings banking can be gained by constructing a balance sheet for the "average" mutual savings bank, obtained by dividing each of the asset and liability items on the consolidated statement for all banks by 528—the total number of mutual savings banks in the country.

THE "AVERAGE" MUTUAL SAVINGS BANK—JUNE 30, 1953

ASSETS	Thous. of dollars	% of total	LIABILITIES	Thous. of dollars	% of total
Cash	$ 1,642	3.3	Deposits	$44,735	89.5
U. S. Gov't securities	17,953	35.9	Other liabilities	424	.8
State & municipal securities	746	1.5	Surplus	4,845	9.7
Other securities	6,059	12.1			
Real estate mortgages	22,653	45.3			
Other loans	299	.6			
Other assets	652	1.3			
Total	$50,004	100.0%		$50,004	100.0%

Compared with other financial institutions which provide facilities for the safekeeping and investment of savings, our "average" mutual savings bank, with $50 million in assets and $45 million in deposits is a large institution. This statistic might be somewhat misleading, however, because the 100 largest banks (less than one-fifth of the total) hold almost three-fourths of all mutual savings bank deposits. Thus the "typical" institution would be much smaller in size.

Deposit accounts are small . . .

A statement of condition can give only a superficial impression of mutual savings banking. Take "deposits" for instance. The statement of condition does not reveal that the average account is about $1,170—thus pointing up the fact that these banks, as has been mentioned, cater to the needs of the small saver. State laws limiting the size of accounts reflect this philosophy. Some sample statutory limits are:

New York $10,000
Connecticut 20,000
Massachusetts 7,500 (for a single-name account; $15,000 for a joint account)
New Jersey 25,000

Eight states, including Pennsylvania and Delaware, set no such limits; but it is common practice for the banks themselves to do so.

. . . and interest payments are moderate in amount

The "average" depositor in our "average" mutual savings bank received an interest-dividend credit of 2.47 per cent on his funds during the first six months of 1953. This rate is about half again as large as that paid at the end of World War II, reflecting both the general rise in money rates that has occurred (the banks are now receiving a higher rate of return on their investments) and increased competition from savings and loan associations and commercial banks. Today's rate is the highest paid since 1937. Although higher than that offered by most commercial banks, it is somewhat lower than the rate paid by many savings and loan associations.

Most deposits are insured

As of the end of last year, 493 (93 per cent) of the 529 mutual savings banks, holding 97.6 per cent of all deposits, participated in some sort of deposit insurance plan. Two hundred and six were

members of the Federal Deposit Insurance Corporation, which insures deposits up to $10,000 per account, and the remaining 287 banks were covered by one of the state plans now in operation in Massachusetts, Connecticut, and New Hampshire. The 188 banks in Massachusetts must be members of the Mutual Savings Central Fund, which insures in full all deposits of member institutions. In Connecticut, 65 of the 72 banks are members of the Savings Banks Deposit Guarantee Fund, which also insures deposits of member institutions in full. Of the remaining banks in Connecticut, four are members of the Federal Deposit Insurance Corporation. The Savings Bank Association of New Hampshire—a voluntary association that functions almost entirely as a deposit insurance institution—has provided protection for all 34 of the mutual savings banks in that state. (In 1953 some of the banks in the state became members of the Federal Deposit Insurance Corporation.)

School savings and savings bank life insurance

Two other services that do not show on the balance sheet deserve mention. The first—promotion of school savings—tends to develop the thrift habit among children of school age, and has the by-no-means-incidental result of creating both good will and future customers for savings banks. At the end of 1952, savings banks held over $63 million of such deposits, representing the savings of over 2 million school children. Most savings bankers agree, however, that operation of a school savings plan is a costly project.

The second service is by no means unprofitable. In the states of Massachusetts, New York, and Connecticut, savings banks are permitted to provide low-cost, over-the-counter life insurance for their depositors. Although the statutory limit per policyholder is small ($5,000 in New York), savings banks in the three states had nearly $700 million of such insurance in force at the end of 1952. Savings bankers argue that by eliminating the insurance salesman on small policies they are providing an important service on an economical basis.

Surplus

For our "average" mutual savings bank, surplus is equal to nearly 10 per cent of assets and almost 11 per cent of deposits. Surplus as a percentage of deposits is significant for several reasons. In the first place, surplus is a "buffer" account—it provides a margin of safety to depositors in case of asset shrinkage; thus losses up to 11 per cent of total deposits could theoretically be absorbed without threatening depositors' rights. In addition, the ratio is significant because some states require that when surplus reaches a certain percentage of deposits, such as 25 per cent, the interest-dividend payment to depositors must be increased.

The ratio of surplus to deposits has taken on much added significance since the passage of the Revenue Act of 1951. For some time there has been a difference of opinion as to the taxing of cooperative enterprises such as mutual savings banks. This Act provided that, for the first time, mutual savings banks would, effective January 1, 1952, be subject to regular corporate income taxes (a maximum of 52 per cent on all but the first $25,000 of net income). Congress, however, tempered the legislation by exempting all income paid as interest-dividends to depositors and all income added to surplus, so long as surplus is no greater than 12 per cent of deposits. Thus any income earned while surplus is more than 12 per cent of deposits, and not paid out as interest-dividends, is subject to the regular corporate in-

come tax (mutual savings banks are fully exempt from excess profits taxes). There is little doubt that the tax as applied will tend to step up interest-dividend payments. It may also stimulate savings banks to invest in tax-exempt issues of state and local governments.

The fact that our "average" bank appears to be well below the 12 per cent limit is decidedly misleading. Published statements of banks are generally ultra-conservative; in the past, funds that would normally be allocated to surplus have been used to write down the value of assets to relatively low levels. Bankers believe that it adds to the prestige of their institution if they can afford to carry on their books a $15 million building at one-fifth of that amount. For tax purposes, however, the "true" values of the assets must be used. This raises the ratio of surplus to deposits and might well pull our "average" bank up into the taxable bracket.

The "bankers' dilemma"

Achieving and maintaining the delicate balance among safety, liquidity, and profitability confronts the management of all financial institutions whose primary role is that of investing other people's money. It is sometimes referred to as the "bankers' dilemma." The nature of the dilemma is simple; but its solution is difficult and varies widely among different types of financial institutions. Simply stated, the problem is that of maintaining the proper degree of safety and liquidity of assets, at the same time earning a return sufficient to attract funds.

The nature of the problem is readily grasped when it is realized that the safest and most liquid of assets—cash—is at the same time the least profitable, while loans and investments that pay the highest rates frequently lack both safety and liquidity. Although a liquid asset is almost invariably a safe one, a safe asset may sometimes not be very liquid.

Compared with commercial banking, the problem of maintaining safety of assets in mutual savings banks is just as important, while that of liquidity is somewhat less pressing since mutual banks have the authority to require about 90 days' notice of withdrawal; however, because for some time now it has been general practice to require little or no withdrawal notice, mutual savings banks attempt to maintain sufficient liquidity to meet withdrawals on demand. Liquidity of assets is therefore by no means an insignificant consideration in the formulation of investment policy.* Finally, investments must be profitable if mutual savings banks are to continue to pay savers a competitive rate that will attract and hold deposits.

Safety first . . .

The nature of savings bank deposits, originating as they do with small savers, makes it even more important that safety be the primary consideration in investment policy. In nearly all of the 17 states in which mutual savings banks operate, therefore, their investments must be selected from lists set up by either the legislature or a supervisory authority. Only two states—Maryland and Delaware—follow the "prudent man" rule under which selection of investments is left primarily to the banks themselves, and even in these states investment portfolios are subject to rigid examination.

State laws regulating the investment of savings bank funds are quite varied. Most states permit investment in United States Government securities, securities of state and local governments, first mortgages on improved real estate (usually limited to a percentage of total assets), mortgages

* To assure a source of liquidity, 23 banks are members of the Federal Home Loan Bank System and three belong to the Federal Reserve System; but these 26 banks hold less than 2 per cent of the assets of all mutual savings banks.

insured or guaranteed by the Federal Housing Administration and the Veterans Administration, and the debt securities of railroads, public utilities, and industrial corporations. Holdings of bonds of business corporations are, in general, subject to a number of limitations and regulations relating to the percentage of assets that can be placed in any one industry, and the past financial record of the particular corporation.

The influence of state regulation and the generally conservative policies of savings-bank management are reflected in the assets, as shown in the balance sheet of our typical bank. Nearly two-fifths of total assets are in the form of cash and United States Government securities. Bonds of public utilities and railroads dominate the "other" securities, which account for about one-eighth of total assets. As can be seen, the largest slice—45 per cent—of assets is in real-estate mortgages, but almost half of these are insured or guaranteed by the Federal Housing Administration and the Veterans Administration, while the remainder are, in most states, written for only 60 to 66-2/3 per cent of the value of the pledged property.

. . . but profitability is important, too

Safety comes first; but mutual savings banks must also strive to make profitable investments, otherwise they will face a gradual loss of funds to competing financial institutions. The drive for earnings is reflected in the large proportion of mortgages held. This percentage has been increasing steadily since the end of World War II, when mortgage loans accounted for less than one-fourth of total assets. Mutual savings banks, in common with other financial institutions, have, during the past eight years, liquidated Government securities in order to obtain funds for other, more profitable types of credit extension. Thus holdings of Government securities relative to total assets have declined steadily from the peak of 63 per cent reached in 1946.

The need for earnings has prompted the banks to petition their state legislatures for authority to invest a portion of their funds in corporate stocks. A few states now permit such investment. For example, Pennsylvania savings banks are now allowed to invest in equity securities an amount not greater than 5 per cent of assets (book value) or 50 per cent of unimpaired surplus, whichever is less. The underlying reason for these moves to increase earnings—namely, the pressure of competition from other financial institutions—is discussed further below.

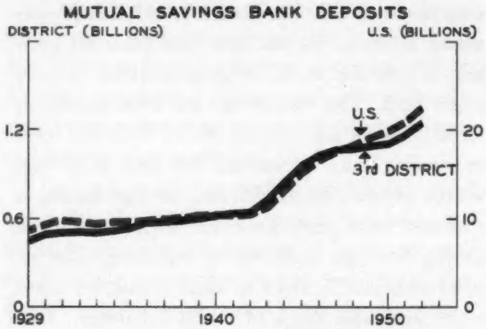
INTERESTED IN INTEREST?

On the 16th of January, 1869, an account was opened at a local mutual savings bank with a $15 deposit. Since that date $2,568 was deposited and $878.93 withdrawn making a net deposit of $1,704.07. The balance on January 1, 1952 was $22,456.37. So that $20,752.30 in interest was earned over the 83 year period.

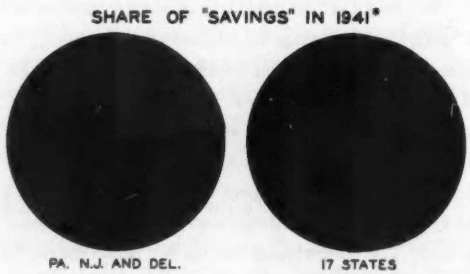
Problems of competition

Since mutual savings banks compete for savings in only 17 states, it would not be accurate to compare them with nation-wide financial institutions. The chart on page 12 shows the trend since 1941 in the 17 states where the banks operate. It shows that savings and loan associations hold a higher proportion of savings deposits than they did pre-war, and that mutual savings banks and commercial banks have lost proportionately. Since the war, however, mutual savings banks have consistently held about 44 per cent of the savings

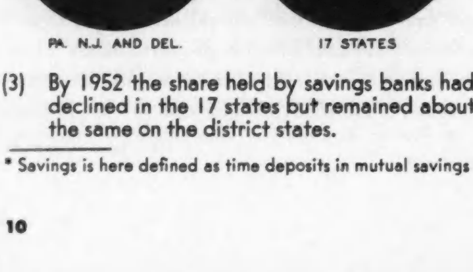
(continued on page 12)



(1) Deposits of savings banks in the district have grown steadily over the past 20 years to keep pace with the national trend



(2) In 1941 local savings banks held a smaller proportion of institutional "savings*" than did those in the 17 states which have mutual savings banks



(3) By 1952 the share held by savings banks had declined in the 17 states but remained about the same on the district states.

SAVINGS BANK

Ten mutual savings banks operate in the Third Federal Reserve District, which comprises the eastern two-thirds of Pennsylvania, the southern half of New Jersey, and all of Delaware. Of the six Pennsylvania banks, four are in Philadelphia, with Johnstown and West Chester boasting one each. New Jersey is represented by two mutual savings banks, one in Trenton and one in Burlington. Both of the Delaware banks are in Wilmington.

Five of the ten district banks are among the 75 largest (in terms of total deposits) in the United States; but there is wide diversity of size among Third District mutual savings banks—both the second largest and second smallest of all such banks in the nation are in this district. For the ten banks combined, total assets amount to $1.4 billion; deposits, $1.2 billion; and surplus, $154 million.

For the three states in the Third Federal Reserve District—Pennsylvania, New Jersey and Delaware—savings deposits in mutual savings banks represent 22 or 23 per cent of total institutional savings (defined here as savings in commercial banks, savings and loan associations, and mutual savings banks.) This proportion of savings held by local mutual savings banks has varied little since 1941. For the 17 states in which savings banks compete, a larger proportion of institutional savings—about 43 per cent—is held in

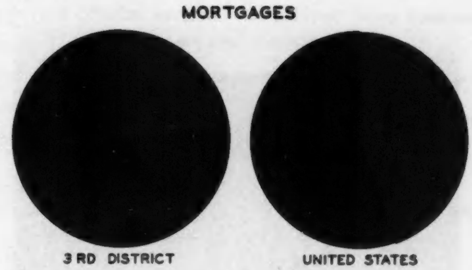
* Savings is here defined as time deposits in mutual savings banks, and commercial banks and shareholdings in savings and loan assoc

IN THE THIRD DISTRICT

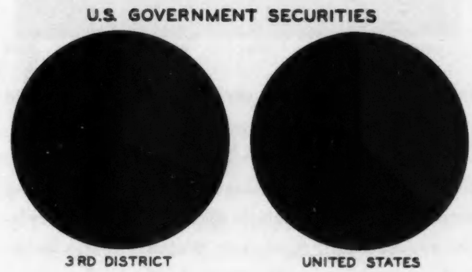
mutual savings banks, but this percentage has declined since 1941.

The most striking fact about the operation of Third District savings banks as compared with the rest of the banks in the United States is the make-up of their investment portfolios. Mutual savings banks in the Third District hold less than one out of every four dollars of assets in the form of real-estate mortgages; the national average is slightly less than one out of two. District banks also hold a smaller proportion of United States Government securities—31 per cent of assets versus 37 per cent for the nation as a whole. Thus the dominant type of investment in this Reserve District is in the category referred to as "other securities," which consist primarily of debt securities of public utilities, railroads, and industrial corporations. It is apparent that savings banks in the Third District channel more funds into business operations—and less to Government and real estate—than do most savings banks in other parts of the country.

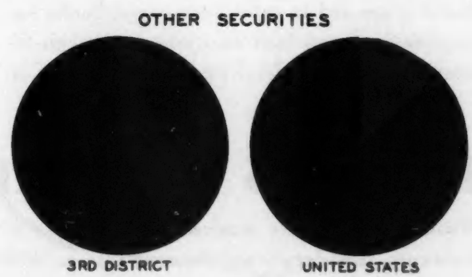
The mutual savings banks in this area are old institutions; five of the ten have passed the century mark, and a sixth reaches it in 1954. The youngest was established in 1890. The many years of successful operations have provided a wealth of experience that should be of great help to these savings banks in meeting the problems of the future.



(4) Mutual savings banks in the district put relatively less funds into mortgages



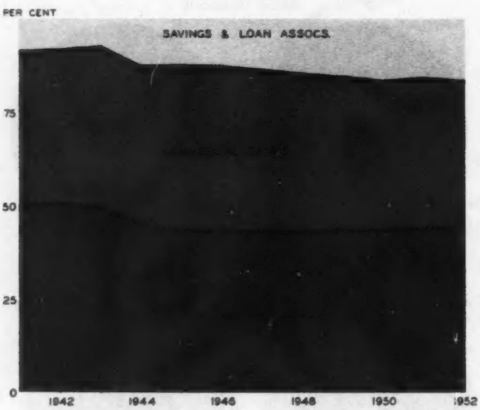
(5) Somewhat less in United States Government securities



(6) And much more into "other" (mostly business securities.)

LONG-TERM SAVINGS IN SELECTED INSTITUTIONS

(Measured in the 17 states in which mutual savings banks operate)



in commercial banks, savings and loan associations, and mutual savings banks.

In the 1930's, mutual savings banks had a distinct competitive advantage because of their long record of safety. This is illustrated by the relative movement of funds into mutual savings banks and away from commercial banks and savings and loan associations during the depression years 1931-1933. Today, the safety of savers' funds is assured in most commercial banks and most savings and loan associations through the operation of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation (the latter does not insure liquidity, however). Mutual savings banks have thus lost an important competitive advantage.

Savings bankers are aware of their position. Recently, they have exerted renewed efforts to extend their services through the establishment of additional branches (the 528 banks now operate 244 branches). Recent attempts to widen the privilege of writing savings bank life insurance have met with failure. More successful have been their attempts to stimulate earnings through a widening of state regulations concerning investments. In some areas, more vigorous advertising has tended to offset some of the competition—but competitors advertise too.

Summary

The 528 mutual savings banks now operating in the United States perform valuable economic functions in stimulating thrift and channeling the savings of the public into productive uses. After 137 years of successful operation, savings banks are now old and respected institutions. Their future, although by no means bleak, is threatened by the growth of competitive institutions. The success with which this competition will be met depends, as always, primarily on the people who make up savings banking—the trustees, the officers and employees, and, by no means to be forgotten, the depositors.

INCOMES IN THIRD DISTRICT STATES

Higher incomes were received by the people of Delaware, New Jersey and Pennsylvania in 1952 than ever before, according to figures recently published by the Department of Commerce. During 1952, income payments to individuals in these states increased five per cent from $27 billion to $28.4 billion. This percentage increase was the same as the gain in the entire country. Delaware, New Jersey and Pennsylvania had increases of six per cent, seven per cent and four per cent respec-

tively. Total payments in the three states combined are now triple the 1940 payments and almost triple the 1929 payments.

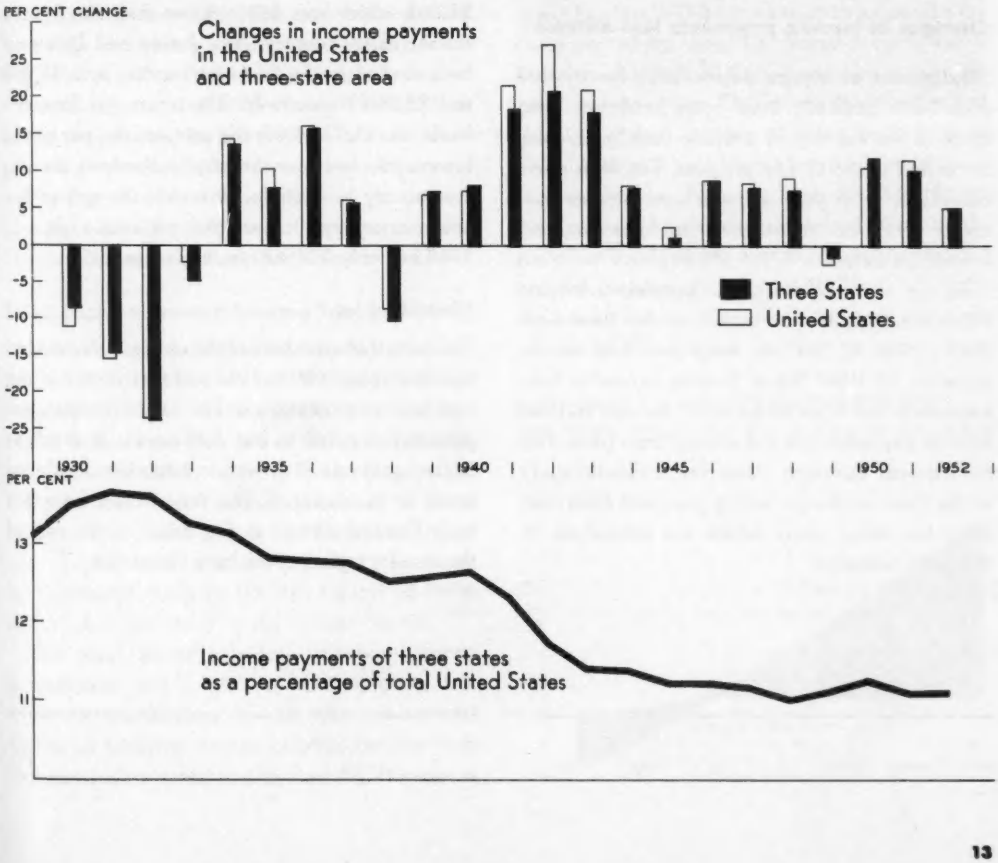
Where income payments* originate, how they fluctuate, and their rate of increase over previous years reflect the kind of local economy we live in.

* These income figures include all payments received by individuals: wages and salaries, proprietors' income (farm and industrial), property income (dividends, interest, net rents and royalties), and "other" income, such as relief, social security, state benefit payments, veterans' pensions and bonuses, and state and local government workmen's compensation and retirement payments.

An industrial area

Income figures for the tri-state area emphasize the advanced industrial development characteristic of the Third Federal Reserve District. Thirty-three per cent of total income was derived from manufacturing payrolls, a considerably higher proportion than in the entire country, where only 24.5 per cent of total income came from that source. Also, a smaller share of income was in the

INCOME PAYMENTS IN THREE STATES (DEL., N. J. AND PA.) AS COMPARED WITH THOSE IN THE UNITED STATES



form of proprietors' profits and a larger share went to employees in the form of wages and salaries. In the three states, 73.2 per cent of all income received was in the form of wages and salaries, compared with only 68.5 per cent in the United States. Conversely, only 10.8 per cent of income in the three states went to proprietors, compared with 15.2 per cent in the United States. Finally, agriculture was much less important in this area as a source of income. Only 1.7 per cent of income here came from agriculture, whereas, 6.7 per cent of the income in the United States came from that source.

Changes in income payments less extreme

Fluctuations of income payments in the tri-state area have generally been more moderate than those in the country as a whole. Last year, both areas had a rise of five per cent, but, with some exceptions from year to year, local income payments increased or declined less than national income payments.

In the years of the great depression, income payments declined less rapidly at the local level than nationally, and the same was true in the recession of 1949. When income payments have increased over a period of years, the rise in local income payments has not usually kept pace with the national increases. However, a careful study of the chart on the preceding page will show that there are many years which are exceptions to this generalization.

Declining share of the nation's income

Despite large gains since pre-war days and the prosperous, twenties, this area has been losing its proportionate share of the nation's income payments. In 1929, the three states received 13.1 per cent of the country's total; in 1952 they accounted for only 11.1 per cent. Their share began to drop in the 30's and in the 40's it declined even more as shown by the chart. However, a significant fact is that since 1945 their share has remained slightly over 11 per cent of total income payments.

Per capita income advantage declines

In 1952 per capita income in the three states was $1,764, which was $125 higher than the figures for the entire country. New Jersey and Delaware both ranked in the first eight states, with $1,959 and $2,260 respectively. The figure for Pennsylvania was $1,710. Over the past decade, per capita income has been consistently higher here than in the country as a whole. However, the spread has been narrowing; it was 16.2 per cent higher in 1940 but only 7.6 per cent higher in 1952.

"Leveling up"

The facts that our share of the nation's income has declined from 1929 to 1945 and that we are losing our relative advantage in per capita income, are probably due, not to our deficiencies as much as to the rapid rate of growth in other less developed areas in the country. The three states have not been "leveled down" to the status of the rest of the country; other areas have "leveled up."

TAX CHANGES AND TAKE-HOME PAY

Personal income taxes are to be reduced and the Social Security payroll tax is to be increased on January 1, 1954. The impact of these changes on consumer incomes and Government receipts is not entirely revealed by the total dollar amounts involved.

According to the Revenue Act of 1951, individual income taxes will be reduced by about 10 per cent all along the line next year. This means that people will pay about $3 billion less in personal income taxes. But also under the present law, wage and salary earners next January 1 will begin to pay 2 per cent Social Security tax on their earnings up to $3,600 a year. The rate now is 1½ per cent on the first $3,600. Self-employed persons covered under the law will pay 3 per cent on the first $3,600, as compared with the present 2¼ per cent. The increase in these payments is expected to come to about $.6 billion.

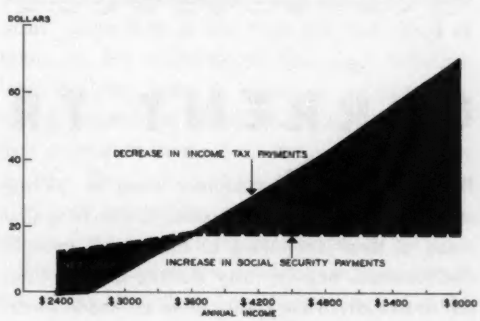
Effects on consumer income and spending

In total dollars, the estimated income tax reduction of $3 billion far exceeds the rise in Social Security payments of about $.6 billion. The favorable balance of $2.4 billion is somewhat misleading, however, in terms of how many people will have their take-home pay increased by these changes. The probability is that for about half of all wage and salary earners the larger slice taken by the Social Security tax will siphon off more dollars than are saved on the income tax cut.

The chart shows how this collision between a reduction and a rise in tax payments will work out for families of four who are covered by Social Security. As can be seen, families with incomes before taxes of less than $3,600—about $70 a week—will find little change or an actual decline in their pay checks. This means that roughly half—the lower half—of all income receivers would notice a decrease or no increase in take-home pay during 1954, since about four out of five workers are covered by Social Security, and since the median income in 1952 was about $3,400.

What the chart does not show, because it is on an annual income basis, is that the tax relief for many families will have most of its impact in the latter part of the year. The Social Security tax is levied on the first $3,600 earned and is not prorated over the year. This means that the head of a family of four earning $4,500 a year or about $87 a week will have his income tax deduction on the weekly pay check cut from $7.13 to $6.44. That represents a saving to him of 69 cents. On the other hand, on his first $3,600 of pay, his Social Security tax will go from $1.31 to $1.74. So that until October, by which time he will have earned $3,600, his net increase in weekly take-

NET EFFECT OF SCHEDULED TAX CHANGES ON TAKE-HOME PAY OF A FAMILY OF FOUR

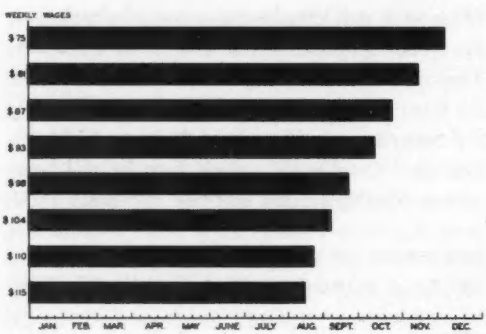


home pay will be only 26 cents. While the over-all income tax reduction is about 10 per cent, the tax cut for families in this income class will mean a saving of just 3.6 per cent over the first nine months or so of the year. For the last three months, this rise will be more than doubled, since no more Social Security tax payments will be required.

The chart below shows the approximate dates next year when workers with various weekly rates will have earned the full $3,600 on which they must pay Social Security tax.

The charts show that the $2.4 billion scheduled to be released to individuals will practically all go to those making in excess of $3,600 a year, and that a portion of this hike in take-home pay will not be effective until the latter months of 1954. Since many lower-income families stand to pay out more in taxes and moderate-income families will receive tax relief in but small amounts late in the year, it seems likely that if tax reduction stimulates any general increase in demand from the "mass market" it will come late in the year.

DURATION OF SOCIAL SECURITY PAYMENTS



Effect on Government receipts

Although, from the standpoint of individuals, the $3 billion income tax reduction will be partially offset by higher Social Security payments, Government budget balancers will miss the entire sum. Funds collected as Social Security payments are not figured in the regular budget, so that the added $.6 billion collected from employees will not be applied to budget receipts. But this money, until needed for payments to individuals, will be made available to the Government through the purchase of Government securities by the Trust Fund.

The higher Social Security tax will also tend to reduce budget revenues. This will come about because Social Security payments by employers on the first $3,600 of each worker's salary are also to be raised from 1½ to 2 per cent, or about $.6 billion. Businesses deduct the Social Security tax as a cost, so that their regular income tax liabilities will tend to be reduced as the Social Security tax is increased.

CURRENT TRENDS

Business forecasters currently seem to be immersed in semantics. The reason, of course, is that many of them are trying to convey the thought that business activity may decline slightly—but not drastically. Fine distinctions are made therefore, among words like "recession", "set-back," "downturn," and so on. Probably the most popular term is "readjustment". In fact, the word is used so frequently that whether or not one agrees with such a forecast, a brief look at what it means

might be worth-while.

In many cases, "readjustment" is used crudely to mean simply "what goes up must come down." In more sensitive hands the word implies that changes are expected which will require adaptation to new conditions. In this sense, of course, it loses much of its impact but at the same time becomes more meaningful. For adjustments are being made all the time in our economy—not so smoothly as textbooks might imply, it is true; but one of the virtues of an economy which relies on freedom in the market place is that adjustments take place rather automatically and impersonally.

These adjustments are not a one-way street. The postwar inflation was an adjustment—a process in which prices corrected an imbalance between pent-up demand and inadequate capacity to produce everything at once. For the past two years or so the economy as a whole has been in relative balance at rather stable prices. Nevertheless, adjustments in specific areas of the economy have been going on constantly. Perhaps the most recent and outstanding example is in agriculture.

Most of the forecasters who use the term "readjustment" recognize all this, of course. But they apparently believe that the over-all level of business activity will decline because adjustments in a number of sectors of the economy will bunch together at the same time. This, they point out, is in contrast to the "rolling adjustments" which prevented the postwar boom from collapsing.

The concept of "readjustment" also implies a change in attitude. Businessmen reflect this when they say that the business environment will be more competitive. They recognize the hard fact that a "readjustment," if and when it comes, may put the less efficient producer out of business. A "readjustment" might also require thinking again in terms of somewhat smaller magnitudes rather than ever-rising indexes of activity.

"Readjustment" comes to the mortgage market

The term "readjustment" has been employed by the Housing and Home Finance Administrator to describe the current situation in the mortgage market. Those in the mortgage business have been much more inclined to use the word "tight." After talking with representative concerns in this Federal Reserve District we conclude that while the market here is tight some improvement is expected shortly.

Apparently, there are no noteworthy instances of builders or mortgage companies holding excessive amounts of completed loans which cannot be disposed of in a secondary market. But both VA and FHA mortgages are selling at discounts of three to four points. Some lenders are completely out of the market for mortgages coming under Government programs. And those who are buying are doing business on a strict quota basis. Furthermore, down payments and maturity requirements are more rigid than formerly. Our reports indicate that advance commitments are very hard to get; frequently they are obtained only by paying a one per cent commitment fee. The situation with respect to conventional financing is said to be somewhat easier, with a 5 per cent rate prevailing.

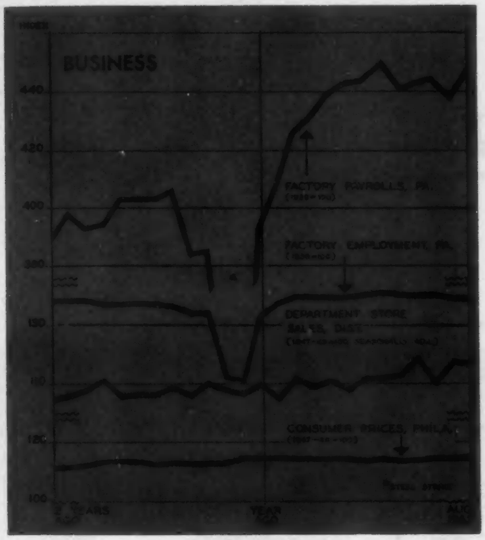
Builders tell us that there are far fewer firm take-out commitments on houses still in the "blue print" stage than at this time last year. Most of them are for conventional financing. Although local builders seem to agree on a continuing strong demand for houses, they nevertheless predict a drop in starts over the next six to nine months. They are acquiring land more slowly now, and proceeding much more cautiously in developing tracts in their possession.

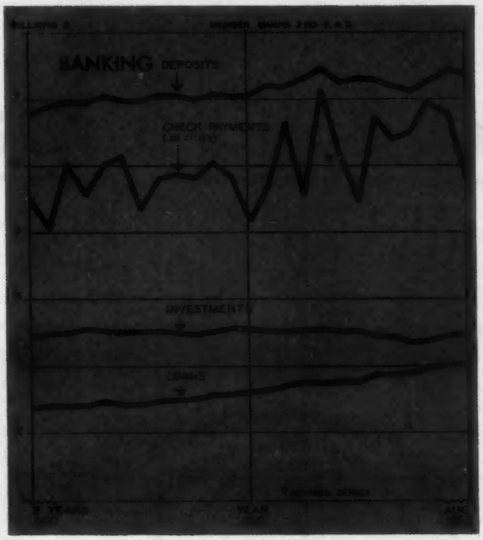
Mortgage lenders are watching the money market closely. And there have been reports that the

recent rise in prices of Government securities and the decline in interest rates have induced some to regard mortgages in a more favorable light. Our latest spot check among a few lenders in this district appears to confirm these reports, but it provides no tangible evidence of an actual change in either the nature or the volume of transactions. Some lenders, who were completely out of the market for VA and FHA mortgages are now said to be at least ready to enter negotiations for this paper. However, advance commitments still seem to be as difficult to obtain as ever.

If the availability of mortgage money does improve as expected, it will be interesting to watch the trend of housing starts in coming months. Those who felt that the recent downward trend was prompted mainly by a shortage of mortgage money will be looking for a revival of activity in home building. On the other hand, those who believed that fewer housing starts reflected something more basic—a weakening of demand—will not be surprised if a downtrend continues in this field.

FOR THE RECORD...



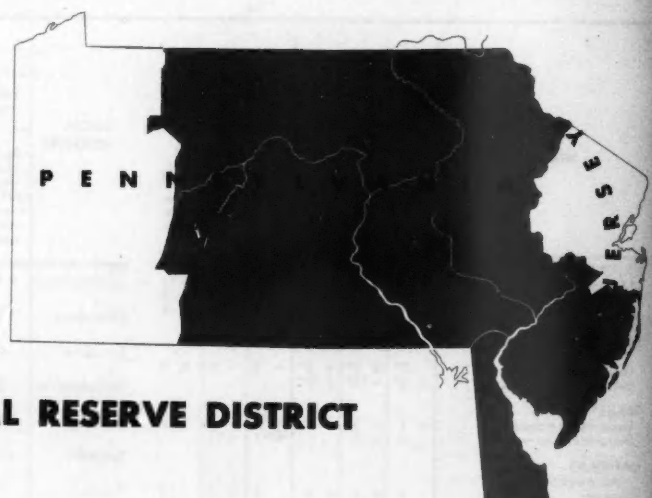


SUMMARY	Third Federal Reserve District — Per cent change: August 1953 from mo. ago	August 1953 from year ago	8 mos. 1953 from year ago	United States — Per cent change: August 1953 from mo. ago	August 1953 from year ago	8 mos. 1953 from year ago
OUTPUT						
Manufacturing production	+ 1*	+ 5*	+ 9*	+ 2	+10	+13
Construction contracts‡	−17	−15	+14	+ 7	− 7	+ 2
Coal mining	− 1	− 5	−15	+13	+14	− 5
EMPLOYMENT AND INCOME						
Factory employment	0*	+ 4*	+ 8*	+ 1	+ 6	+ 8
Factory wage income	+ 2*	+14*	+18*	...	...	...
TRADE**						
Department store sales	− 1	+ 5	+ 4	− 2	− 2	+ 3
Department store stocks	0	+ 8	...	+ 1	+11	...
BANKING (All member banks)						
Deposits	− 1	+ 4	+ 4	0	+ 3	+ 3
Loans	0	+15	+14	+ 1	+10	+11
Investments	0	− 3	− 3	− 1	0	− 1
U.S. Govt. securities	0	− 4	− 3	− 1	0	− 2
Other	0	0	+ 1	+ 1	0	+ 4
Check payments	−14§	+12§	+12§	− 9	+10	+ 8
PRICES						
Wholesale	...	...	...	0	− 1	− 2
Consumer	0†	0†	+ 1†	0	+ 1	+ 1

*Pennsylvania †Philadelphia §20 Cities
**Adjusted for seasonal variation. ‡Based on 3-month moving averages.

LOCAL CHANGES	Factory* Employment — Per cent change August 1953 from mo. ago	year ago	Factory* Payrolls — Per cent change August 1953 from mo. ago	year ago	Department Store Sales — Per cent change August 1953 from mo. ago	year ago	Department Store Stocks — Per cent change August 1953 from mo. ago	year ago	Check Payments — Per cent change August 1953 from mo. ago	year ago
Allentown	+1	+1	+4	+ 5	...	...	...	...	− 6	+ 5
Harrisburg	+2	+1	+3	+ 4	...	...	...	...	−11	+ 7
Lancaster	0	+7	0	+15	− 2	+ 4	+ 2	+ 9	− 9	0
Philadelphia	0	+5	+1	+11	+ 9	+ 6	+10	+ 7	−13	+14
Reading	+1	+2	+1	+11	+ 8	+ 9	+ 4	+10	−10	+22
Scranton	+1	+1	0	+ 6	...	...	...	...	− 7	+ 3
Trenton	−1	+5	−6	+12	− 4	−12	+ 2	+ 4	−47	+ 9
Wilkes-Barre	+1	0	+2	+ 1	+22	+ 9	+ 2	+ 7	− 5	+24
Wilmington	+5	+9	−2	+18	− 3	− 9	+ 9	+ 4	−18	− 3
York	+1	+7	+3	+20	+15	+12	+ 4	+15	+ 3	+38

*Not restricted to corporate limits of cities but covers areas of one or more counties.



THIRD FEDERAL RESERVE DISTRICT